

## Message Text

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SUBJECT: MRS. CARTER'S VISIT OF JUNE 3-6: ECONOMIC HIGHLIGHTS

REF: LIMA 4619

1. SUMMARY: THIS CABLE REPORTS ON GENERAL THRUST OF MEETINGS HELD BY ASSISTANT SECRETARY TODMAN, AMBASSADOR AND OTHERS WITH KEY GOP CABINET MINISTERS AND SENIOR GOP OFFICIALS AT WHICH PRIMARILY ECONOMIC MATTERS DISCUSSED, E.G. FOREIGN MINISTRY BREAKFAST SATURDAY JUNE 4, AND PRIVATE MEETING AT RESIDENCE WITH FINANCE MINISTER AND PRESIDENT OF CENTRAL BAN SAME EVENING. END SUMMARY.

2. DURING THE COURSE OF MRS. CARTER'S JUNE 3-6 VISIT TO PERU, WE HAD OCCASION TO DISCUSS COUNTRY'S ECONOMIC SITUATION FULLY AND FRANKLY WITH SENIOR GOP OFFICIALS. ONE MAJOR OPPORTUNITY WAS BREAKFAST AT TORRE TAGLE JUNE 4, HOSTED BY FOREIGN MINISTER DE LA PUENTE, AND INCLUDING FINANCE MINISTER PIAZZA, HEAD OF CENTRAL BANK SANTISTEVAN, ASSISTANT SECRETARY TODMAN, AMBASSADOR, ROBERT PASTOR, EMBASSY'S E/C COUNSELOR, AND OTHER KEY OFFICIALS. ANOTHER OPPORTUNITY WAS EARLY EVENING MEETING AT RESIDENCE ATTENDED BY AS TODMAN, AMBASSADOR, PIAZZA, SANTISTEVAN, E/C COUN, AND TWO TOP  
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FINANCE MINISTRY ADVISORS, FELIX NAVARRO AND JORGE CAMET.

3. FOREIGN MINISTER DE LA PUENTE CONCENTRATED ON EXPRESSING PERUVIAN VIEWS ON NEW INTERNATIONAL ECONOMIC ORDER (NIEO) ALONG QUITE FAMILIAR LINES, I.E. THE NEED TO RESTRUCTURE PRESENT ECONOMIC ORDER TO TAKE INTO ACCOUNT DESIRE OF DEVELOPING WORLD TO PARTICIPATE MORE FULLY IN TRANSFORMATION PROCESS OF RAW MATERIALS, TRANSPORTATION, AND SERVICES. WHILE RECOGNIZING UNDERTAKINGS BY INDUSTRIALIZED COUNTRIES TO MAKE INCREASES IN DEVELOPMENT LOANS, HE NOTED THAT THIS

WAS NOT IN ITSELF A SOLUTION, AND, INDEED, IT HAS THE LONG-RANGE EFFECT OF WORSENING PERU'S EXTERNAL DEBT STRUCTURE. THE FOREIGN MINISTER EXPRESSED AN INTEREST IN THE CREATION OF A COMMON FUND TO FACILITATE THE CREATION OF COMMODITY BUFFER STOCKS. HE SEEMED TO FAVOR A UNITARY APPROACH ON COMMODITY ISSUES IN GENERAL, WITH THE COMMON FUND SET UP TO SUPPORT A NUMBER OF PRODUCTS. HE MENTIONED (WITHOUT PRESSING) THE DEVELOPING WORLD'S INTEREST IN INDEXING RAW MATERIALS EXPORT PRICES TO RISING COSTS OF IMPORTS FROM THE INDUSTRIAL WORLD. HE STRESSED NEED FOR DEVELOPING AND DEVELOPED WORLD TO ACT IN CONCERT TODAY TO AVOID CONFLICT TOMORROW.

4. MINISTER OF FINANCE PIAZZA'S COMMENTS WERE FAR MORE SHARPLY FOCUSED ON PERU'S PRESENT ECONOMIC DIFFICULTIES. HE FRANKLY RECOGNIZED THAT PERU WAS IN A RECESSIONARY PHASE WITH BALANCE OF PAYMENTS AND INFLATIONARY PROBLEMS, AND THE NEED FOR A SHARP SERIES OF AUSTERITY MEASURES TO AID IN ECONOMIC STABILIZATION. HE MENTIONED THE NEED FOR AN END TO FUEL PRICE SUBSIDIES (WITH GASOLINE PRICES GOING UP AT THE PUMP, BUT IN AN INCREMENTAL WAY TO AVOID PUBLIC DISTURBANCES), SELECTIVE BUDGET CUTS (E.G. NO CUTS IN THE EDUCATION BUDGET, WHERE 80-90 PERCENT OF THE BUDGET IS FOR SALARIES), BETTER BUDGETARY CONTROL OF MILITARY PURCHASES, A DRAMATIC IMPROVEMENT IN PERU'S ECONOMIC DATA-GATHERING ABILITY, A SETTING OF PRIORITIES FOR PUBLIC SECTOR INVESTMENTS, A CONTINUATION OF MINI-DEVALUATIONS, AND OTHER LIMITED OFFICIAL USE LIMITED OFFICIAL USE

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MEASURES. PIAZZA NOTED THAT WHILE IN THE LONGER RUN PERU'S WELL-DIVERSIFIED ECONOMY AND GROWING SELF-SUFFICIENCY IN PETROLEUM SUGGESTED A BRIGHTER FUTURE, IN THE MIDDLE TERM SUBSTANTIAL BRIDGE FINANCING WOULD BE REQUIRED. IN THIS REGARD, MEMBERS OF THE GOP ECONOMIC TEAM EXPRESSED THE HOPE, AND THE BELIEF, THAT THE ECONOMIC MEASURES TO BE ADOPTED BY PERU IN THE VERY NEAR FUTURE WOULD SATISFY THE IMF TEAM WHICH IS DUE TO ARRIVE HERE THE THIRD WEEK IN JUNE.

5. PIAZZA AND HIS TEAM AGREED WITH THE AMBASSADOR THAT THE IMF COMMENTS WHICH WERE SO UNFORTUNATELY PUBLISHED IN THE WEEKLY PRESS IN PERU IN FACT AMOUNTED TO A FIRST NEGOTIATING POSITION, AND THAT THE FUND COULD BE EXPECTED TO BE MORE REASONABLE AS DISCUSSIONS CONTINUED. WHILE RECOGNIZING THAT THE IMF PLAYS A SALUTARY ROLE IN POINTING OUT DIFFICULTIES, IT IS VITAL THAT THE FUND SHOW A REASONABLE AWARENESS OF POLITICAL REALITIES IN DEVELOPING COUNTRIES. LPHESE REMRRKS BROUGHT DISCUSSIONS AROUND TO WHAT WAS OBVIOUSLY THE KEY POINT WHICH PIAZZA AND SANTISTEVAN WISHED TO MAKE -- THAT THE U.S. COULD BE MOST HELPFUL TO PERU AT THIS MOMENT IF IT STRESSED TO APPROPRIATE FUND OFFICIALS THE NEED TO SHOW AN APPROPRIATE AWARENESS OF THE REALITIES OF THE PERUVIAN SCENE. ASSISTANT SECRETARY TODMAN SAID HE UNDERSTOOD THIS POINT OF

VIEW, AND NOTED THAT HE HAD ENCOUNTERED SIMILAR PROBLEMS IN OTHER COUNTRIES OF THE DEVELOPING WORLD. HE ADDED HE WAS IN REGULAR TOUCH WITH IMF OFFICIALS IN WASHINGTON.

6. MEETINGS ALSO TOUCHED ON GROWING RECOGNITION BY GOP OF NEED FOR STIMULATING PRIVATE FOREIGN DIRECT INVESTMENT, WHICH IS SOMEWHAT FACILITATED BY NEW CHANGES IN ANDEAN PACT CODE. FOREIGN INVESTMENT SHOULD BE IN AREAS OF HIGH DEVELOPMENTAL PRIORITY AND SHOULD MEET OTHER GOP CRITERIA. "RULES OF THE GAME" SHOULD BE SPELLED OUT CLEARLY. WITH RESPECT TO DEVELOPMENT PRIORITIES, AMBASSADOR SUGGESTED NEED TO CONCENTRATE SCARCE RESOURCES IN AREAS WHICH WILL PRODUCE EXPORTS SOONER RAHTER THAN LATER, THUS GENERATING FURTHER REVENUES FOR LIMITED OFFICIAL USE  
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FURTHER DEVELOPMENT. SOME ACTIVITIES RELATED TO FOREIGN INVESTMENT SUCH AS BRIBERY, SKEW DEVELOPMENT PRIORITIES AND SLOW DOWN DEVELOPMENT, AMBASSADOR NOTED, RECALLING U.S. EFFORTS TO ACHIEVE AN INTERNATIONAL CODE OF CONDUCT FOR MULTI-NATIONAL CORPORATIONS. GOP OFFICIALS TENDED TO BE CRITICAL OF "DONOR" IN THESE BRIBERY CASES, BUT AMBASSADOR POINTED OUT THAT THE PERSON WHO ASKS FOR A BRIBE IS AT LEAST EQUALLY GUILTY, AND THAT IN ANY CASE THE PRACTICE SHOULD BE DISCOURAGED IN EVERY POSSIBLE WAY.

7. AMBASSADOR RAISED WHAT HE DESCRIBED AS "INDISCREET" QUESTION CONCERNING HOW PIAZZA PLANNED TO CONTROL MILITARY PURCHASES. AMBASSADOR NOTED THAT NO MATTER HOW WELL THE ECONOMY DID, THERE WOULD BE NO IMPROVEMENT IN THE LOT OF THE AVERAGE PERUVIAN IF HARD-EARNED MONEY WENT INTO NON-PRODUCTIVE MILITARY HARDWARE. PIAZZA NOTED THAT MAJOR ECISIONS OF PERU'S NATIONAL SECURITY HAD TO BE MADE BY RANKING MILITARY, BUT THAT HE WAS INSISTING THAT MILITARY SIT DOWN AND BUDGET SUCH PURCHASES CAREFULLY IN ADVANCE. AS TODMAN NOTED THAT A COUNTRY COULD WEAKEN ITSELF IN THE LONG RUN BY OVER-BUDGETING FOR MILITARY ITEMS AT THE EXPENSE OF CAPITAL GOODS AND EVEN FOODSTUFFS.

8. IN VIEW IMPORTANCE OF THESE RECENT MEETINGS, PRINCIPAL POINTS REPORTED ABOVE WERE DISCUSSED WITH SANTISTEVAN BY ECONOMIC/COMMERCIAL COUNSELOR JUNE 6. SANTISTEVAN CONFIRMS THAT PARAS 3-7 ABOVE ACCURATELY REFLECT CURRENT THINKING GOP ECONOMIC TEAM.

9. COMMENT: WE WERE AL ENCOURAGED BY THESE FRANK DISCUSSIONS, AND BY THE COURAGEOUS WAY THAT PIAZZA AND HIS TEAM ARE INSISTING ON NEEDED ECONOMIC MEASURES (PIAZZA TELLS US HE CARRIES HIS RESIGNATION IN HIS COAT POCKET"). WE BELIEVE THAT THE PIAZZA TEAM, INCLUDING THE CENTRAL BANK, IF FIRMLY DETERMINED TO PUT THROUGH A SERIES OF MEASURES WHICH SHOULD MEET IMF STAND-BY CRITERIA, AND, MORE IMPORTANTLY, HELP

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TO STABILIZE THE PERUVIAN ECONOMY.

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